

FDIC State Profile

Summer 2004

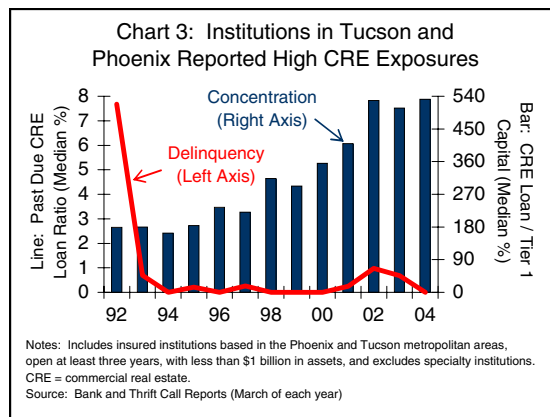
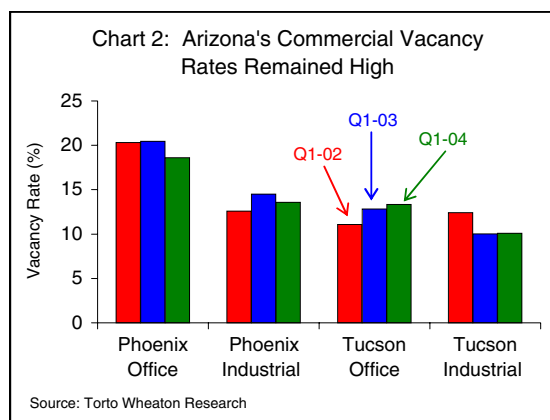
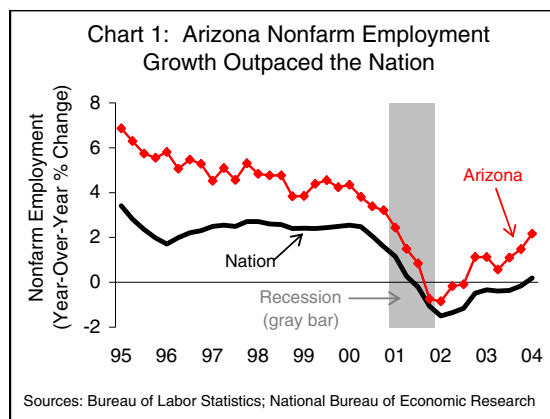
Arizona

Arizona's employment picture gained strength through first quarter 2004, ranking third among the states in job growth.

- Year-over-year, payroll jobs in the state increased 2.2 percent, outperforming the nation (See Chart 1). Employment growth in the construction, retail trade, and several services sectors offset losses in the information, manufacturing, and wholesale trade industries.
- During the same one-year period, computer and electronic products manufacturing jobs (which include semiconductors) declined 7.2 percent, information services jobs decreased 3.9 percent, and aerospace products and parts manufacturing jobs sank 2.1 percent. Despite job losses, these industries may be well positioned to rebound given the positive reports of increased business spending on information technology and government defense spending.

Office, industrial, and multifamily vacancy rates in the Phoenix and Tucson MSAs remained above pre-recession levels, but some sectors may be stabilizing.

- According to *Torto Wheaton Research* (TWR), Phoenix's office and industrial vacancy rates declined in the year ended first quarter 2004, to 18.6 percent and 13.6 percent, respectively (See Chart 2).
- TWR reported rising year-over-year vacancy rates in the Tucson office market, but stable conditions in the industrial market during the same time period.
- Apartment vacancy rates in both markets also remained well above pre-recession levels. Between fourth quarter 2002 and fourth quarter 2003, TWR estimates that multifamily vacancy rates deteriorated from 8.4 percent to 9.1 percent in Phoenix, but improved slightly from 8.7 percent to 8.3 percent in Tucson.
- Weak market conditions could adversely affect institutions headquartered in the Phoenix and Tucson MSAs holding CRE¹ loans. As of first quarter 2004, the median CRE loan-to-Tier 1 capital ratio among established community



¹ CRE loans include construction, multifamily, and nonfarm-nonresidential mortgages.

State Profile

institutions² based in these MSAs increased to 531 percent, nearly double the 283 percent median concentration reported by similar metropolitan institutions nationally (See Chart 3).

- The group's median construction and development (C&D) loan-to-Tier 1 capital ratio increased to 161 percent by first quarter 2004, significantly higher than the 52 percent median ratio reported by MSA-based established community institutions nationwide.
- Increasing CRE vacancy rates affected past-due CRE loan ratios mildly among Phoenix- and Tucson-based established community institutions in early 2002, although delinquencies appeared to moderate as interest rates declined through 2004.

Home sale and construction activity were strong during 2003, but could slow prospectively.

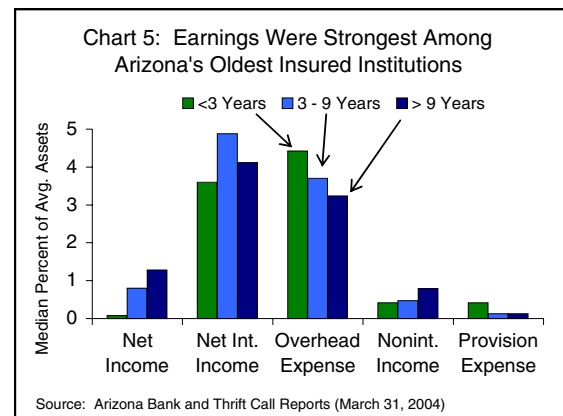
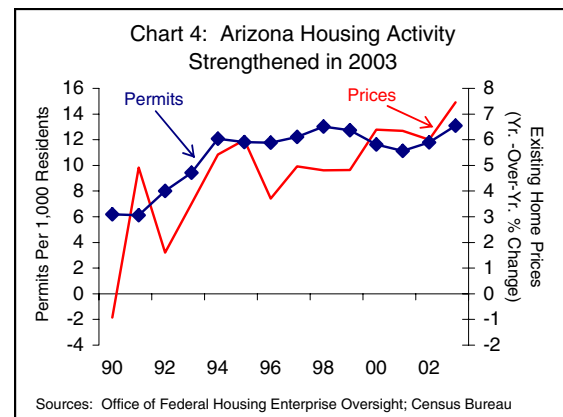
- According to the *Office of Federal Housing Enterprise Oversight*, existing home prices grew 7.5 percent year-over-year in fourth quarter 2003. Residential construction also boomed. Arizona authorized permits on 13 new housing units per thousand residents last year, the second highest rate of any state in the nation (behind Nevada) and twice the per-capita rate of residential construction reported nationally (See Chart 4).
- Rising construction input costs could pressure builder cash flows, in particular should home sales volumes slow or housing appreciation decelerate. In March 2004, softwood lumber and steel producer price indices were up 24 percent and 16 percent, respectively, relative to year-earlier levels.

Earnings among Arizona's insured institutions continued to improve through first quarter 2004.

- The year-to-date median return-on-assets (ROA) ratio was 0.80 percent in March 2004, moderately lower than 0.82 percent in early 2003, and below the 1.02 percent national median. The median net interest margin expanded year-over-year while lower relative overhead, loan-loss provisions, and tax expense also supported profitability.
- Earnings performance was weaker among institutions less than nine years old, which accounted for nearly two-thirds of the state's insured institutions (See Chart 5). Older insured institutions reported strong ROA ratios, in part because many specialized in high-yielding consumer lending.

Arizona-based institutions reported elevated noncore³ funds and brokered deposit dependence.

- Roughly 43 percent of Arizona-based insured institutions reported brokered deposit exposures at March 31, 2004, a far higher proportion than the 24 percent reported nationally. Jumbo and brokered deposits could prove volatile or increasingly expensive should competing equity market investments improve or interest rates rise.
- However, among the state's insured institutions, the median noncore funds-to-total asset ratio declined moderately to 16.4 percent over the past year, after showing a steady increase over the past decade.



²Established community institutions are defined as insured institutions holding less than \$1 billion in total assets and open at least three years, excluding industrial loan companies and specialty institutions.

³Noncore funds include brokered deposits, jumbo time deposits, foreign office deposits, and other borrowed funds such as Federal funds purchased and reverse repurchase agreements.

Arizona at a Glance

General Information	Mar-04	Mar-03	Mar-02	Mar-01	Mar-00
Institutions (#)	49	49	44	48	47
Total Assets (in thousands)	49,516,184	49,916,372	42,727,288	63,905,130	53,971,228
New Institutions (# < 3 years)	13	15	12	16	14
New Institutions (# < 9 years)	32	31	25	26	26
Capital	Mar-04	Mar-03	Mar-02	Mar-01	Mar-00
Tier 1 Leverage (median)	9.96	9.60	9.41	8.72	9.45
Asset Quality	Mar-04	Mar-03	Mar-02	Mar-01	Mar-00
Past-Due and Nonaccrual (median %)	0.58%	0.56%	1.05%	0.87%	1.09%
Past-Due and Nonaccrual >= 5%	1	1	4	4	2
ALLL/Total Loans (median %)	1.10%	1.21%	1.36%	1.33%	1.19%
ALLL/Noncurrent Loans (median multiple)	3.09	2.71	2.20	2.83	2.75
Net Loan Losses/Loans (aggregate)	4.10%	3.60%	4.35%	2.04%	1.88%
Earnings	Mar-04	Mar-03	Mar-02	Mar-01	Mar-00
Unprofitable Institutions (#)	8	10	13	14	8
Percent Unprofitable	16.33%	20.41%	29.55%	29.17%	17.02%
Return on Assets (median %)	0.80	0.82	0.75	1.08	0.93
25th Percentile	0.15	0.12	-0.19	-0.18	0.36
Net Interest Margin (median %)	4.59%	4.36%	4.99%	5.11%	5.36%
Yield on Earning Assets (median)	5.91%	6.08%	7.14%	8.92%	8.83%
Cost of Funding Earning Assets (median)	1.17%	1.50%	2.05%	4.04%	3.52%
Provisions to Avg. Assets (median)	0.16%	0.20%	0.23%	0.16%	0.22%
Noninterest Income to Avg. Assets (median)	0.54%	0.75%	0.67%	0.68%	0.71%
Overhead to Avg. Assets (median)	3.86%	3.98%	4.09%	4.31%	4.44%
Liquidity/Sensitivity	Mar-04	Mar-03	Mar-02	Mar-01	Mar-00
Loans to Deposits (median %)	90.73%	85.61%	81.68%	77.09%	77.79%
Loans to Assets (median %)	73.10%	68.33%	68.55%	65.09%	65.94%
Brokered Deposits (# of Institutions)	21	22	15	14	9
Bro. Deps./Assets (median for above inst.)	7.12%	8.08%	15.04%	8.97%	14.32%
Noncore Funding to Assets (median)	16.37%	18.17%	14.00%	16.13%	12.53%
Core Funding to Assets (median)	65.79%	64.07%	64.95%	70.01%	73.47%
Bank Class	Mar-04	Mar-03	Mar-02	Mar-01	Mar-00
State Nonmember	28	25	19	19	21
National	15	17	16	18	16
State Member	2	3	6	7	6
S&L	0	0	0	0	0
Savings Bank	4	4	3	4	4
Stock and Mutual SB	0	0	0	0	0
MSA Distribution	# of Inst.	Assets	% Inst.	% Assets	
Phoenix-Mesa AZ	34	44,515,203	69.39%	89.90%	
Tucson AZ	5	3,510,503	10.20%	7.09%	
Las Vegas NV-AZ	4	1,148,833	8.16%	2.32%	
Yuma AZ	3	204,468	6.12%	0.41%	
No MSA	2	84,804	4.08%	0.17%	
Flagstaff AZ	1	52,373	2.04%	0.11%	